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IN THE

Supreme Court of the United States

OCTOBER TERM, 1976

No. 76-391

MORAINE PRODUCTS, *Cross-Petitioner,*

v.

ICI AMERICA INC., *Cross-Respondent.*

Cross-Petition for a Writ of Certiorari to the United States Court of Appeals for the Seventh Circuit

BRIEF FOR CROSS-RESPONDENT IN OPPOSITION

SIGMUND TIMBERG
815 15th Street, N.W.
Washington, D.C. 20005

ARTHUR G. CONNOLLY
CONNOLLY, BOVE & LODGE
1800 Farmers Bank Building
Wilmington, Delaware 19899

Attorneys for Petitioner
ICI America Inc.

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BRIEF FOR CROSS-RESPONDENT IN OPPOSITION

QUESTION PRESENTED

Whether a patent license agreement granting a license which is exclusive except as to the licensor and another licensee, under which the exclusive licensee is not authorized to license third parties, has such "a pernicious effect on competition" and is so "lacking in any redeeming virtue" that it, standing by itself, may be conclusively presumed to be *per se* unreasonable under Section 1 of the Sherman Act.

STATEMENT OF THE CASE

Much of the material in cross-petitioner Moraine's Statement of the Case is completely irrelevant to its *per se* Sherman Act violation theory.[1] This irrelevant material is couched in conclusory language reflecting counsel's version of evidence that must, under the Circuit Court's ruling, be presented to the jury,[2] and evaluated by it in conjunction with other evidence the parties desire to adduce. ICI America has therefore undertaken not only to restate the Question Presented but also to supply its own Statement of the Case.

On January 19, 1961, Plough entered into a patent license agreement with Atlas, granting to Atlas the right to use the Feinstone Patent. This license was exclusive, except as to Plough itself and as to Block Drug Company, to which Plough subsequently granted a license on August 25, 1961. Under the agreement

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[1] A good example of such irrelevant material is Moraine's assertion, in a footnote on page 5 of its cross-petition, that the District Court in the Detroit action in which the Rider Patent was held invalid found that Atlas had engaged in misconduct with respect to the Rider Patent. The 6th Circuit reversed the District Court on the issue of Atlas' alleged misconduct, *Atlas Chemical Industries, Inc.* v. *Moraine Products*, 509 F.2d 1, 7 (6 Cir. 1974)—a fact that the cross-petition has seen fit to ignore. See ICI America App. 46a-47a. (References to "ICI America App." are to the appendix in ICI America's Petition for Certiorari in No. 76-390). When Moraine tried to reassert this charge upon return of the case to the District Court in Detroit, the case was dismissed.

[2] See the discussion of two other factors deemed by Moraine to be material to this Court's consideration but which ICI America regards as extraneous to the *per se* question raised by Moraine, Point II, *infra*, pp 8 to 11.

Atlas did not have the right to sublicense the Feinstone Patent in the United States. See App. A2-A3, fn. 3.[3]

Moraine's cross-petition (pp. 2-3) erroneously describes the Plough-Atlas license agreement as follows: "Their license agreement provided that no other licenses would be granted without their joint consent." The license agreement contained no such "joint consent" provision concerning further licensees. Indeed, by limiting licensees to only Block and Atlas, the agreement itself expressly negated all future licensees.[4]

Moraine's cross-petition also incorrectly states (p. 5) that any drug company "wishing to market a product employing simethicone for treating gas in humans required a license under both patents", i.e., the Feinstone Patent and Moraine's Rider Patent No. 3,442,189 on which Moraine bases this lawsuit. It is not correct to say that such company "required" a license under Moraine's Rider Patent. The Rider Patent was narrow in scope, having only process claims and no product claims. Hence, any person making or selling a simethicone-containing product for treating gas in humans that employed a process other than that claimed by the Rider Patent was free to do so without securing a license under the Rider Patent. Moreover, even where possibly infringing processes may be involved, it is

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[3] References to "App." are to the Appendix of Moraine's cross-petition herein.

[4] As will be set forth in Point III, pp. 11 to 12, *infra*, the possibility of granting further licenses could stem only from the parties' consent, in subsequent bargaining, to the termination of the exclusive license. The possibility of such termination is, of course, present in all license agreements, but it is not a provision of the Plough-Atlas agreement.

doubtful that a simethicone product manufacturer or seller would have sought a license under the Rider Patent, which was attacked in court as invalid within the first year of its life, and was adjudicated to be invalid about three and a half years after its issuance in the declaratory judgment action brought by Atlas in Detroit (see ICI America's petition for certiorari (No. 76-390), pp. 3-4, and p. 4, fn. 2).[5]

Moraine urged in the District Court that the Plough-Atlas agreement constituted a *per se* violation of § 1 of the Sherman Act (15 U.S.C. § 1) and, in the alternative, that under the "rule of reason" approach the contract between, and the conduct of, Atlas and Plough constituted an unreasonable restraint of trade.

At the close of Moraine's case, the District Court directed a verdict against Moraine on both theories of recovery, see ICI America App. 1a to 3a. Moraine's suit against Plough was settled shortly after the directed verdict. Upon a stipulation entered into between Moraine and Plough, the District Court entered an order dismissing the complaint as to Plough with prejudice. Thereafter Atlas was the only defendant remaining in the case.

On appeal, Moraine again argued the *per se* illegality of the Plough-Atlas license agreement and that, even if there was no *per se* violation, there was sufficient evidence to take the case to the jury under the "rule of reason" theory. The Seventh Circuit affirmed

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[5] ICI America's petition for certiorari, filed herein on September 15, 1976, sets forth its position that Moraine's present action, since it is founded on an attempt to obtain royalties on the Rider Patent, should be dismissed because of the judicial invalidation of that patent in the Detroit action, regardless of the issue raised by Moraine in its cross-petition.

the District Court's conclusion that the Plough-Atlas agreement was not a *per se* antitrust violation. But it reversed in part and ordered a new trial, on the basis that there was evidence in the record which warranted submitting to the jury the issue whether ICI America had unreasonably restrained commerce under the "rule of reason". See App. A25-A26.[5a]

ARGUMENT

I. The Decision Below on the Per Se Violation Issue Is Correct

This Court, in *Northern Pacific Railway Co.* v. *United States,* 356 U.S. 1, 5 (1958), laid down the rule, confirmed in *United States* v. *Topco Associates,* 405 U.S. 596, 607 (1972), that only those agreements or practices can be considered to be *per se* unreasonable under the Sherman Act—

> "which because of their pernicious effect on competition and lack of any redeeming virtue are conclusively presumed to be unreasonable and therefore illegal without elaborate inquiry as to the precise harm they have caused or the business excuse for their use."

The only issue presented by this cross-petition is whether the Plough-Atlas agreement of January 19, 1961, is a *per se* antitrust violation, a view that was rejected by the two Courts below (App. A2, A3, A6). Under this agreement, Plough gave up the lawful monopoly to which its ownership of the Feinstone Patent entitled it and granted licenses to two competitors, Atlas and Block. Any licensing arrangement which thus expands the number of competitors on the

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[5a] The Seventh Circuit's opinion is reported in 538 F.2d 134 (1976).

market can hardly be characterized as having a pernicious effect on competition.

Even the two cases most heavily relied on by Moraine acknowledge that an exclusive (or semi-exclusive) license [6] such as is involved here may be valid and may confer the right to exclude others from the field covered by the patent, see *United States* v. *Besser Mfg. Co.*, 96 F. Supp. 304, 311 (E.D. Mich. 1951); *United States* v. *Krasnov*, 143 F. Supp. 184, 200 (E.D. Pa. 1956). Since there is no provision for compulsory licensing in the Patent Code, a patentee may in the usual case validly decline any requests for a license that are made to him.

There are plausible legal and economic justifications for a patentee limiting the number of licenses it grants in any particular licensing program. As the Court below noted (App. A19):—

> "Economic analysis suggests that the licensor's business interest is often not advanced by licensing all applicants. * * * A licensor is not always able to recoup the profits surrendered to competing licensees, Adelman & Juenger, *supra* at 298, and it is not difficult to see that the apprehension of such a possibility would exert influence upon the decisions of sophisticated businessmen."

As long as there are licensors who limit the number of their licenses on such a rational basis, semi-exclusive

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[6] The court below correctly observed that an exclusive license may involve more than a single licensee. App. A8. See, *in accord*, *McCullough Tool Co.* v. *Well Surveys, Inc.* 343 F.2d 381, 404-405 (10 Cir. 1965), one of the cases relied on by Moraine in its cross-petition. However, to eliminate a semantic confusion that occurs in some of the cases, we shall refer to the Plough-Atlas agreement and similar license agreements limiting the number of licensees to two or three as "semi-exclusive" licenses.

licenses of the Plough-Atlas type cannot be said to have a "pernicious effect on competition" and to be *per se* illegal.

A noteworthy example of a semi-exclusive license, set forth at length in the opinion of the Court below, is the Salk Patent Licensing Plan. Under this plan the Salk Institute, the patentee, committed itself to limit its initial licensing to no more than two U. S. firms (App. A9-A11). The plan received a "business review" clearance from the Justice Department. We do not argue, as Moraine's cross-petition wrongly anticipates (see p. 11, footnote *), that the Justice Department's intention not to oppose the Salk Licensing Plan makes it lawful or provides any antitrust immunity for the activities involved. But, as the Court below noted, it does establish that there are circumstances in which semi-exclusive licenses may be "the least anti-competitive way" to develop a drug on reasonable terms, and may be "reasonable because [the patentee] had been unable to obtain license agreements with qualified and interested firms without such a limitation" (App. A11). This demonstration was strong enough to override, and is more significant than, the Justice Department's prior abstract pronouncements about the illegality of semi-exclusive licenses.

It does not matter that Salk is a differently circumstanced licensor than Plough or that the limitation to two U.S. licensees is in effect for a three year period, during which lead time, incidentally, the two licensees can become firmly entrenched on the U. S. market. A *per se* antitrust rule is general in nature and industry-wide in scope. Differences among licensors and in the duration of the restraint are immaterial and inconsequential to a *per se* rule.

As shall be pointed out next, the record below made by the parties is barren of any reference as to the general impact of semi-exclusive licenses on competition. But the clearance given the Salk Plan is strong indication that semi-exclusive licenses of the Plough-Atlas type in fact have a "redeeming virtue", do not necessarily have a "pernicious effect on competition" and hence are not *per se* unreasonable under the Sherman Act, see *Northern Pacific Railway Co.* v. *United States,* quoted *supra* at p. 5.

The foregoing, taken in conjunction with the fact that the decision of the Court below does not conflict with applicable decisions either of this Court or of the lower federal courts (see Point III, pp. 11 to 14, *infra*), establishes that the decision of the Court below on the *per se* issue is correct.

II. The State of the Record Below Does Not Justify Review by This Court

To compensate for the absence of any factual base in the record for an inference of *per se* antitrust violation, Moraine stresses, in its Questions Presented and Statement of the Case, a basic assumption that has not only been controverted by the parties, but is not material to the consideration of its *per se* violation question, contrary to the Rules of the Supreme Court of the United States, Rule 23(e), Moraine's cross-petition (see pp. 2, 5) assumes that the relevant commercial market in this case is that of products employing simethicone for treating flatulence in humans, and thus concludes, all too easily, that Plough and Atlas have monopolized that market. Its asserted basis for this assumption is that simethicone is the only product that has been found by the Food and Drug Administration to be effective as an antiflatulent.

However, the FDA report on which Moraine relies (Antiflatulent Products for Over-the-Counter Human Use, 21 C.F.R. 332) does not, in ICI America's view, support Moraine's contention that simethicone-containing antiflatulents are a relevent market susceptible of being monopolized or illegally restrained.[7] Rather it indicates that the relevant market is the much broader one of products that can serve as an " 'antiflatulent' and/or 'to alleviate or relieve the symptoms of gas in humans' " (*id.*, 332.30(a)). The FDA, in a subsequent announcement initiating a new program to study this area, indicated that there are, in addition to simethicone, 48 drug ingredients (including those contained in Warner-Lambert's well-known Rolaids and Gelusil)[8] which may fall within this broadly defined field, see 40 Fed. Reg. 38179, dated August 27, 1975.

Moreover, the FDA report on Antiflatulent Products has no bearing at all on the competitive situation at the times involved in Moraine's complaint, which was filed on September 23, 1970. The FDA findings were not made final until June 4, 1974 (39 Fed. Reg. 19877), almost four years later. At no time has there been any restriction on the freedom of the many companies in the broad drug market referred to in the preceding paragraph to include, in their labelling and promotional literature, statements concerning the

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[7] The District Court recognized that this complex issue as to the scope of the relevant market remains to be tried and resolved by the jury, see ICI America App. 2a.

[8] That these drugs compete with Plough's and Atlas' antiflatulents was testified to at the trial by a Warner-Lambert witness and by Moraine's own economist, see Transcript of Hearing before Judge Thomas R. McMillen, March 24 and 27, 1975, pp. 741, 1215, 1227 and Plaintiff's Exhibits 335(a) and 335(b).

efficacy of their drugs as alleviators and relievers of gas in humans, including the treatment of such symptoms as distension, fullness, bloating or pressure associated with gas. In fact, such statements were made by Atlas' competitors, see Transcript of Hearing before Judge Thomas R. McMillen, March 24, 1975, pp. 725-729.

Another matter stressed in Moraine's cross-petition is its erroneous statement (p. 4) that over forty drug companies "requested licenses under the Feinstone Patent from the defendants". It cannot properly be said that these companies "requested licenses", since most of these communications were mere inquiries. More significantly, as the Circuit Court recognized, these inquiries are material, not to Moraine's *per se* violation question, but to the possibility of a jury inference "that Atlas combined with Plough in forcing other simethicone-containing products off the market" (App. A24).

If Moraine's case depends on this Court's acceptance either of Moraine's definition of the relevant market or of its appraisal of Plough's and Atlas' conduct with respect to inquiries about the Feinstone Patent, then it clearly has no *per se* case, because any ruling based on either of these two limiting factors could not conceivably have industry-wide application.

Moreover, this Court should not review this case because the record below (a) contains no evidence concerning the general effect of semi-exclusive patent licenses on competition, and (b) even with respect to two points deemed material by Moraine, is currently quite incomplete and remains to be developed and presented

to the jury. As the Court below properly observed (see App. A17):—

> "The record in this appeal does not give the court the information it would need in order to undertake the kind of economic and policy analysis which should properly undergird any determination to add to the pantheon of prohibited per se practices."

III. There Is No Conflict of Decision

Moraine's basic argument is that the decision of the Court below that exclusive or semi-exclusive licenses are not *per se* illegal conflicts with those reached by the lower federal courts in the six cases cited on page 8 of its cross-petition. The Court below, after an examination of those cases, disposed of this argument by concluding that

> "none of them is controlling on the question of per se illegality. *Krasnov* involved pooling of patents, price fixing and the institution of punitive infringement suits for the purpose of harrassment rather than with the intention that they be adjudicated on the merits. In *Besser,* the conspiracy involved pooling of patents, an agreement to pool future improvement patents, interlocking directorates, the use of improper influence on suppliers or competitors to curtail their output, and recklessly made threats of suit. Each of the leading cases cited by Moraine in support of its theory of per se illegality involved a broad spectrum of anti-competitive conduct on the part of the defendants" (App. A8-A9).

On pages 9 and 10 of its cross-petition, Moraine, on the basis of quotations from *Besser, Krasnov* and two other decisions taken out of context, argues that the Plough-Atlas agreement is *per se* illegal, because it requires the "joint consent" of the patentee and its li-

censee before other licenses can be granted and that this gives the licensee a "veto power" in the selection of other licensees and is therefore *per se* illegal.

To this it may be said that it is true of an exclusive patent license agreement (as it is true of any contract) that the parties to the agreement must give their "joint consent" before the contract can be amended or modified, and that the licensee may in that sense be said to have a "veto power" over activities of the licensor that are in conflict with the terms of the contract. But this clearly is not the type of "joint consent" or "veto power" with which the courts in the *Besser-Krasnov* line of cases were concerned. Rather, as already pointed out (see page 6, *supra*), *Besser* and *Krasnov* recognized that exclusive licenses [9] may be valid and that such licenses may confer the right to exclude others from the field. Obviously, in the case of a semi-exclusive license such as the Plough-Atlas agreement, before any new license can be granted, the license has to be modified by the "joint consent" of the parties, in which sense both the licensor and the licensee may be said to have "veto power". However, it is difficult to see how the operation of this elementary principle of contract law can convert a valid into an invalid agreement.

The licenses condemned in the *Besser-Krasnov* line of cases were not simple exclusive or semi-exclusive licenses, but involved situations where it was clear from evidence outside the license that "the parties intended [the] contract to be a means whereby control of the

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[9] It was pointed out earlier (see page 6, footnote 6, above) that the term "exclusive license" includes "semi-exclusive" licenses of the Plough-Atlas type. In any event, Moraine's fallacious "joint consent" theory applies regardless of whether the patent license is limited to one or two licensees.

industry could be acquired and competition eliminated", see *United States* v. *Besser Mfg. Co.*, 96 F. Supp. 304, 311 (E.D. Mich. 1951); see in accord, *United States* v. *Krasnov*, 143 F. Supp. 184, 199 (E.D. Pa. 1956). Also, they concerned situations where two or more

> "individual patentees combine their valid patent monopolies and contract between themselves and with their licensees to secure mutual benefits for themselves and their licensees that are not given to them by the patent laws, and which agreement gives to the opposite patentee and the licensees a right of control over patent rights that may be asserted, and is used in restraint of interstate trade and commerce", *Mason City Tent & Awning Co.* v. *Clapper*, 144 F. Supp. 754, 768 (W.D. Mo. 1956); *Clapper* v. *Original Tractor Cab Co.*, 165 F. Supp. 565, 577 (S.D. Ind. 1958). Cf., in accord, *McCullough Tool Co.* v. *Well Surveys, Inc.*, 343 F. 2d 381, 405-407 (10 Cir. 1965).

The parties to these agreements "were jointly given an exclusive market and control thereover by the terms of said Agreement, and not singularly as a consequence of patent privileges acquired". See *Clapper* v. *Original Tractor Cab Co., supra*, at 576.[10]

Plough, the assignee of the Feinstone Patent, in granting a semi-exclusive license under a single patent to two licensees, was clearly asserting in its 1961 license agreement with Atlas a right which it has under the patent laws to limit its licensing activity (see pages 6

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[10] ICI America fails to see the pertinence of *United States* v. *Associated Patents, Inc.*, 134 F. Supp. 74 (E.D. Mich. 1955), a case involving a "specialized cartel", where five competing manufacturers of machine tools formed a patent-holding company for the purpose of allocating exclusive fields of manufacture to each other.

to 8, *supra*). Plough has not embarked on any patent pooling program with competitors. Atlas' and Block's rights under the 1961 agreement flowed directly from Plough's "privilege" as the assignee of the Feinstone Patent. Moreover, the Plough-Atlas agreement does not confer, upon a non-exclusive licensee or other person not possessing a relevant privilege under the patent laws, any right to restrict or control its patent licensing or enforcement activity, with a view to controlling an industry or fixing prices or curtailing output or doing anything else contrary to the Sherman Act.

Accordingly, if Moraine has any claim that Plough and Atlas violated the antitrust laws, it is not by virtue of the Plough-Atlas agreement, but can only be, as the Court below pointed out, with respect to "conduct incidental" to that agreement (App. A3). This being the case, the Plough-Atlas agreement cannot be considered *per se* violative of the Sherman Act.[11]

The foregoing makes it clear that the Plough-Atlas agreement, taken by itself, represents a decision by Plough to limit the exploitation of its single lawful patent monopoly to three persons, Atlas, Block and itself. Since the agreement itself shows no purpose to eliminate or suppress industry competition through the misuse of patent rights, the six Supreme Court decisions cited on pages 7 and 8 of the Moraine cross petition, reflecting antitrust truisms that no one would dispute, are inapplicable to this case. There is therefore no conflict among the decisions.

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[11] Moraine practically admitted as much when it included, in its Statement of the Case, an extended reference to over 40 alleged "refusals" to license under the Plough-Atlas agreement, see page 10, *supra*.

IV. Moraine's Second Question Is Insubstantial and Inconsequential

Moraine has raised as the second Question Presented in its cross-petition the following:

> "Can commercial misconduct which is a per se antitrust violation in one line of commerce not be a per se violation simply because it occurs in another line of commerce?"

This question is self-contradictory and lacking in substance, because a rule of *per se* antitrust violation is necessarily industry-wide in scope. The appropriate response to Moraine's pointless question is that commercial misconduct which is *not* a *per se* antitrust violation in any line of commerce (e.g., drugs) cannot be a *per se* violation at all.

Moraine's second Question seems to be based on its misreading (see p. 12 of its cross-petition) of the Seventh Circuit's purpose in referring to the literature on the patent licensing problems of the drug industry. The Court turned to this literature not to create any special status for the drug industry, but because it recognized the need for information as to the competitive impact of the challenged restriction on the affected drug market and felt that there was nothing in the record before it that would give it the needed information (App. A16-A17), see page 11, *supra*. This vacuum in the record is why the clearance given the Salk Patent Licensing Plan figures so importantly in the Court's opinion (see pp. 7 to 8, *supra*), and why the Court canvassed the relevant literature on patent licenses in the drug industry before concluding that the Plough-Atlas agreement was not a *per se* antitrust violation.

CONCLUSION

For the foregoing reasons, it is respectfully submitted that this Cross-Petition for a Writ of Certiorari should be denied.

Respectfully submitted,

SIGMUND TIMBERG
815 15th Street, N.W.
Washington, D.C. 20005

ARTHUR G. CONNOLLY
CONNOLLY, BOVE & LODGE
1800 Farmers Bank Building
Wilmington, Delaware 19899

Attorneys for Petitioner
ICI America Inc.

October 14, 1976

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